

Lease agreements that contain purchase options that are equal to the fair market value of the tangible personal property at the end of the lease term are considered true leases, and the lessors incur Use Tax liability on their cost price of tangible personal property purchased for rental purposes. See 86 Ill. Adm. Code 130.2010. (This is a GIL.)

December 8, 1998

Dear Mr. Xxxxx:

This letter is in response to your letter that we received on August 25, 1998. The nature of your letter and the information you have provided require that we respond with a General Information Letter which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

COMPANY manages the tax administration for several leasing companies conducting business in your state. Our company is not conducting any business in your jurisdiction but our clients lease equipment within your state. The leased equipment consists of computers, machinery, furniture and motor vehicles. Some of our clients do have a physical location within the state while others do not.

Currently we are implementing state tax guidelines to conform to existing sales/use/rental tax laws and would like clarification of the tax treatment of the different types of lease agreements recognized by your state. **First**, could you please list and define the various leases subject to the collection of sales/use/rental tax. For each different type of lease, could you answer the following questions:

- = Is tax collected and submitted at the beginning of the lease (upfront) or collected and submitted as each lease payment becomes due?
- = What type of tax (sales, use or rental) should be used if tax is submitted at beginning of lease?
- = What type of tax (sales, use or rental) should be used if tax is submitted when each payment becomes due?
- = If collected upfront, how is the taxable base calculated?

**Second**, could you please send any documentation, state statutes or any literature that would assist our company in applying these state sales/use/rental tax-filing requirements to our clients. I also understand your state publishes a regular newsletter, periodic tax rate changes and other material used in determining the proper application of your sales/use/rental tax rules. Our company would like to be included on a regular mailing list to receive your sales/use/rental tax changes. Could this be arranged?

Thank you for your time. If you have any questions please call me at #####.

For general informational purposes we enclose a copy of 86 Ill. Adm. Code 130.2010, the Department's regulation that covers the taxation of leases. Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation and Use Tax purposes. Lessors are subjected to a Use Tax on their cost price or acquisition value of tangible personal property which they use by leasing in Illinois. This means lessors encounter a front-end tax on value rather than an amortized tax on receipts. The only exception is automobiles rented for one year or less.

True leases generally have no buy out provisions at the close of the leases. If buy out provisions do exist, they must be fair market value buy out options in order to maintain the character of the true leases. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See, 86 Ill. Adm. Code 130.220(a). As end users of tangible personal property located in Illinois, lessors incur Use Tax liability on their cost price of such property.

Under Section 130.2010(a), persons who purport to "lease" the use of property, but in fact sell such tangible personal property to nominal "lessees," are considered to be making conditional sales subject to Retailers' Occupation Tax. Such would be the case when the agreements contain nominal purchase options at the end of the lease term. Such transactions are considered conditional sales from the outset, and all the receipts from the transaction would be subject to tax. In these situations Retailers' Occupation Tax is due on all the payments received by the "lessors," and for automobiles the tax on all payments is due at the start of the lease term when the motor vehicle must be titled in Illinois.

Lessors or rentors of motor vehicles are considered to be retailers when they sell automobiles coming off lease. Section 1c of the Retailers' Occupation Tax Act (35 ILCS 120/1c) provides, in part, that "A person who is engaged in the business of leasing or renting motor vehicles to others and who, in connection with such business sells any used motor vehicle to a purchaser for his use and not for the purpose of resale, is a retailer engaged in the business of selling tangible personal property at retail." Therefore, when lessors sell an automobile to lessees, the lessors will incur Retailers' Occupation Tax liability on the gross receipts from such sales.

Automobiles leased under terms of one year or less in Illinois are not subject to Use Tax but rather are subject to the Automobile Renting Occupation and Use Tax. (35 ILCS 155/1 et seq. ). This tax is imposed at the rate of 5% of the gross receipts from such business, and local auto rental taxes may also apply.

If you wish to obtain a complete copy of the Illinois Sales and Use Tax Rule Book you can remit \$6.50 to this office, attention Margaret Forth. Individual rules can be downloaded off the Department's World Wide Web site. The Department occasionally sends out informational bulletins to registered taxpayers and practitioners. To obtain further information on receiving bulletins that explain the Department's administration of the Illinois tax laws you can contact the Department's Taxpayer Information Division or you can access the Department's Web site.

I hope this information is helpful. The Department of Revenue maintains a Web site which can be accessed at [www.revenue.state.il.us](http://www.revenue.state.il.us). If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Karl Betz  
Associate Counsel

KB:msk  
Enc.